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LINDA S. GREEN, CHAPTER 11 TRUSTEE

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

In re)	
	)	Case No. 10-13730
SUPERIOR ACQUISITIONS, INC.	)	(Chapter 11)
)	
Debtor.	)	A.P. No. 11-1034
_____)	
	)	MEMORANDUM OF POINTS AND
DMRG, LLC, a California	)	AUTHORITIES IN SUPPORT OF
limited liability company;	)	MOTION TO DISMISS COMPLAINT
	)	PURSUANT TO F.R.Civ.P. 12(b)(6)
Plaintiff,)	
v.)	
	)	Hearing Date: April 1, 2011
LINDA S. GREEN, Chapter 11 Trustee of	)	Time: 9:00 a.m.
the Estate of Superior Acquisitions, Inc.;	)	Santa Rosa Courtroom
SUPERIOR ACQUISITIONS, INC.)	
)	
Defendants)	
_____)	

INTRODUCTION

This complaint is properly resolved by a dispositive motion because it turns on a discreet legal issue. That is, does an “absolute assignment of rents” executed in connection with a secured real estate loan divest the borrower of ownership rights in the rental income ? As will be shown below, the answer to that question is clearly “no.” That being the case, the instant complaint must be dismissed.

1 **FACTUAL ALLEGATIONS OF THE COMPLAINT**

2 As of the filing of the petition for relief the Debtor Superior Acquisitions, Inc. owned
3 various real property, including two office buildings located at 43467 Highway 299E, Fall
4 River Mills, CA and 965 Parallel Dr., Lakeport, CA (Complaint, p. 2:26- p.3:3). Both
5 properties were separately rented by the Debtor to the California Department of Motor Vehicles,
6 (*id* p.4:19 -p. 5:6).

7 The properties were subject to separate prepetition notes secured by first deeds of trust in
8 favor of Umpqua Bank. Concurrently with the deeds of trust, the Debtor executed a recorded
9 “Assignment of Rents” for each property, (*id*, p.4:4-17). Plaintiff DMRG, LLC purports to be
10 the assignee of the subject loans, deeds of trust, and assignment of rents, (*id*, p. 6).

11 The form “Assignment of Rents” are identical for each loan. The documents state in
12 relevant part:

13 “For valuable consideration, Grantor hereby assigns, grants a
14 continuing security interest in, and conveys to Lender all of
15 Grantor’s right, title, and interest in and to the Rents from the
16 following described Property.....

 This is an absolute assignment of Rents made in connection with
an obligation secured by property pursuant to California Civil
Code section 2938...” (Complaint, Exhibits F and G).

17 As of October, 2009, the Debtor defaulted on both loans and the lender made a direct
18 demand for turnover of the rents (Complaint, p. 5:8 - p. 6:2).

19 In November of 2010, two months *after* the filing of the petition for relief, the DMV
20 turned over a total of **\$90,800** in back rents to the Plaintiff (*id*, pp. 7-8). The Complaint admits
21 that the Debtor and the Trustee have demanded a turnover of these post petition collections, but
22 the Plaintiff has refused to do so (*id*, p. 8:6-16).

23 The first and second claims for relief seeks a declaratory judgment that these post petition
24 collections are the property of DMRG, not the Estate. The third claim for relief demands
25 turnover of any post-petition rents collected by the Estate. The fourth claim for relief seeks to
26 enjoin the Estate’s use of post-petition rents, also based on the claim that DMRG, not the Estate,

1 is the owner of these rents. (*id*, pp. 8-11).

2 **ARGUMENT**

3 **1. THE COMPLAINT MUST BE DISMISSED BECAUSE IT IS**
4 **ENTIRELY BASED ON THE ERRONEOUS LEGAL**
5 **THEORY THAT THE LENDER IS THE OUTRIGHT**
6 **OWNER OF RENTAL INCOME FROM THE ESTATE'S**
7 **REAL PROPERTY**

8 **A. California Civil Code Section 2938 Nullifies**
9 **"Absolute" Assignment of Rents Clauses**

10 DMRG admits that the Estate still owns fee title to the subject real property. DMRG
11 claims that it, not the Estate, owns the rental income from the subject real property, due to the
12 "absolute" assignment of rents "pursuant to California Civil Code Section 2938" contained in
13 Exhibits F & G.

14 This meritless contention can be promptly refuted by an examination of Civil Code
15 Section 2938(a), the statute referred to in the document. It states:

16 A written assignment of an interest in leases, rents, issues, or
17 profits of real property made in connection with an obligation
18 secured by real property, **irrespective of whether the assignment**
19 **is denoted as absolute**, absolute conditioned upon default,
20 additional security for an obligation, or otherwise, shall, upon
21 execution and delivery by the assignor, be effective to create a
22 present security interest in existing and future leases, rents, issues
23 or profits of that real property....(Emphasis added)

24 Lest there be any remaining doubt, 1 Bernhardt *California Mortgage & Deed of Trust*
25 *Practice*, 4th Ed. (CEB 2010) Section 6.25, p. 419 explains:

26 Under the current CC Section 2938, an assignment of rents
executed on or after January 1, 1997, made in connection with an
obligation secured by real property gives the assignee a present
security interest in the rents "irrespective of whether the
assignment is noted as absolute, absolute conditioned upon default,
additional security for an obligation, or otherwise." **Thus, as of**
January 1, 1997, a literally enforceable absolute or conditional
absolute assignment of rents may no longer be
created....(Emphasis added).

Bernhardt further cautions at *id* Section 6.26:

...the careful practitioner should treat any rents provisions (even

1 those created before 1997) as requiring some form of enforcement
2 step and should act accordingly (generally by seeking a
receivership).

3 Civil Code Section 2938 makes it quite clear that DMRG has not acquired outright
4 ownership of the Estate's rental income. As it states elsewhere in the subject "Assignment of
5 Rents", all DMRG acquired was a "...continuing *security interest* in, all of Grantor's right, title,
6 and interest in and to the Rents..." (Complaint, Exs. F & G). Plaintiff is a lienholder, not an
7 owner.

8 **B. Plaintiff's Purported Ownership Claims Are**
9 **Further Nullified By Bankruptcy Code Section**
10 **541(a)(6)**

11 Bankruptcy Code Section 541(a)(6) states in relevant part:

12 The commencement of a case...creates an estate. Such estate is
13 comprised of all of the following property, wherever located and
14 by whomever held:
(6) Proceeds, product, offspring, rents, or profits of or from
property of the estate, except as are earnings from services
performed by an individual debtor after the commencement of the
case.

15 The effect of this statute on a purported "absolute" assignment of rents clause was the
16 subject of *In re Amarvathi Partnership*, 416 BR 618 (Bankr. S.D. Tex. 2009). In that case a
17 Chapter 11 debtor filed a motion to use cash collateral, consisting of rental income from an
18 apartment complex. Like the Plaintiff DMRG in the instant case, the secured creditor objected,
19 arguing that due to an "absolute" assignment of rents clause contained in the deed of trust
20 the rental income was not "collateral", it was the lender's property outright. Unlike the situation
21 here, such an argument was supported by Texas law. In a lengthy, scholarly decision, the
22 bankruptcy court rejected the lender's claim, holding that the unambiguous language of Section
23 541(a)(6) preempts any contrary state law. The court held that the rents were merely "cash
24 collateral" and proceeded to authorize the debtor to use the cash collateral pursuant to Section
25 363. See also *In re Vienna Park Properties*, 976 F.2d 106, 114 (2d. Cir. 1992) and *In re*
26 *Wheaton Oaks Officer Partners Ltd. P'ship*, 27 F.3d 1234, 1240 (7th Cir. 1994).

1 Pursuant to the plain text of Section 541(a)(6) the rental income from the Debtor's
2 property is property of the estate, not property of the Plaintiff DMRG.

3 **CONCLUSION**

4 Plaintiff DMRG's ownership claim in the rental income arising out of the Estate's real
5 property is directly contrary to both California law and the Bankruptcy Code. Its complaint is
6 wholly without merit, and should be dismissed.

7
8 Dated: March 3, 2011

MacConaghy & Barnier, PLC

9
10 /s/ JohnH. MacConaghy

John H. MacConaghy

Attorneys for Defendant and Counter-claimant

11 LINDA S. GREEN, CHAPTER 11 TRUSTEE
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